

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 19586
[REDACTED])	
)	DECISION
Petitioner.)	
_____)	

[Redacted] (petitioner) protests the Notice of Deficiency Determination issued by the auditor for the Idaho State Tax Commission (Commission) dated June 23, 2006. The Notice of Deficiency Determination asserted an additional liability for Idaho income tax, penalty, and interest in the total amounts of \$2,008, \$1,947, and \$1,861 for 2001, 2002, and 2003, respectively.

The petitioner filed federal income tax returns for the years in question but did not file Idaho income tax returns. The auditor used the petitioner's federal income tax returns as a basis for determining the petitioner's liability.

The petitioner was a married man during the years in question. He filed his federal income tax returns claiming the filing status of head of household. The auditor changed his filing status from head of household to married filing separately. The petitioner did not protest this adjustment.

The petitioner raised several issues on which he disagreed with the auditor's determination:

1. The denial of claimed losses from rental property,
2. The disallowance of medical expenses as itemized deductions,
3. The disallowance of personal property tax as an itemized deduction,
4. The disallowance of charitable contributions as charitable contributions, and
5. The assertion of penalties as a part of the deficiencies referred to above.

The petitioner alleges that he held a trailer for rental during the years in question. He reported no income from the property but claimed expenses in the total amounts of \$5,225, \$10,469, and \$6,615 for 2001, 2002, and 2003, respectively. The auditor denied the claimed losses and stated:

When an individual owns a dwelling unit and uses it for both personal and rental purposes, deduction of expenses is limited. A dwelling unit is considered to be used as a residence if the individual owner's use of the unit (or a portion of it) for personal purposes exceeds the longer of (1) 14 days, or (2) 10% of the period of rental use. If a dwelling unit is rented for less than 15 days a year, the owner can't deduct any of the rental expenses, but is not taxed on any of the rental income. (IRC § 280A)

The auditor further stated that, "if an activity is not engaged in for profit, then the related deductions are allowed only to the extent of the income from the activity. (IRC § 183)"

The petitioner contends that he did not use the property for personal purposes. On the other hand, he had signed a "Homeowner's Exemption Application" in 2000 indicating that he was the owner/occupant and used this property as his primary dwelling place as of January 1 [2000]. Based on his application, the exemption was granted. If the property was not the petitioner's primary dwelling but instead was rental property, he would not have been entitled to the exemption. However, the petitioner did not ask that the exemption be rescinded. This would indicate that he did live in the property.

Whether the petitioner occupied the property in question as his primary dwelling is not clear from the facts in the file. However, this is not relevant to the Commission's ultimate conclusion that the petitioner is not entitled to the claimed rental losses.

If the petitioner used the property as his personal residence, Internal Revenue Code § 280A(g) precludes the claimed losses:

(g) Special rule for certain rental use. Notwithstanding any other provision of this section or section 183, if a dwelling unit is used during the taxable year by the taxpayer as a residence and such dwelling unit is actually rented for less than 15 days during the taxable year, then –

- (1) no deduction otherwise allowable under this chapter because of the rental use of such dwelling unit shall be allowed, and
- (2) the income derived from such use for the taxable year shall not be included in the gross income of such taxpayer under section 61.

Since the petitioner had no income from the property, none of the deductions would be allowable.

If the petitioner did not use the property as a residence, then the Commission finds that the claimed losses are precluded pursuant to Internal Revenue Code §183. Internal Revenue Code § 183 stated, in pertinent part:

Activities not engaged in for profit.

(a) General rule.

In the case of an activity engaged in by an individual or an S corporation, if such activity is not engaged in for profit, no deduction attributable to such activity shall be allowed under this chapter except as provided in this section.

(b) Deductions allowable.

In the case of an activity not engaged in for profit to which subsection (a) applies, there shall be allowed–

(1) the deductions which would be allowable under this chapter for the taxable year without regard to whether or not such activity is engaged in for profit, and

(2) a deduction equal to the amount of the deductions which should be allowable under this chapter for the taxable year only if such activity were engaged in for profit, but only to the extent that the gross income derived from such activity for the taxable year exceeds the deductions allowable for reason of paragraph (1).

(c) Activity not engaged in for profit defined.

For purposes of this section, the term "activity not engaged in for profit" means any activity other than one with respect to which deductions are allowable for the taxable year under section 162 or under paragraph (1) or (2) of section 212.

Treasury Regulation 1.183-2 sets out factors to be considered in determining whether a particular activity is “an activity not engaged in for profit.” In considering these factors, the Commission finds that the petitioner was not engaged in the activity for profit. Of particular concern to the Commission is the lack of advertising of the subject property. The petitioner contends that he had placed a sign or signs indicating that the property was for rent. With regard to the signs, there had been some indication that the property as a whole, or in some part, would not be available for 60 days. The petitioner did not contend that he had listed the property for rent with any agency or that he had purchased ads for the rental of the property in any publication.

In two cases involving the rental of a condominium in Hawaii by a couple from Oklahoma, the same taxpayers were in court twice concerning losses from the same condominium for different years. The first time involved the taxable years of 1970 and 1971. Edith G. and James R. McKinney v. United States, No. CIV-76-805T (W.D. Okla. November 23, 1977). The second time involved the taxable years of 1974, 1975, and 1976. McKinney v. Commissioner, T.C. Memo 1981-181. In the latter case, the taxpayers prevailed. They purchased their condominium in Hawaii in November of 1966. The operating results were as follows:

<u>Year</u>	<u>Rental Income</u>	<u>Cash Expenses Excluding Depreciation</u>	<u>Total Depreciation</u>	<u>Net Profit (or Loss) (Including Depreciation)</u>
1966	\$ 550.00	\$ 1,529.07	\$ 1,888.25	\$ (2,867.32)
1967	5,375.00	6,330.52	2,506.95	(3,462.47)
1968	4,673.75	8,110.97	2,482.61	(5,919.83)
1969	1,518.80	4,755.45	2,884.27	(6,120.92)
1970	936.00	6,016.65	2,409.94	(7,490.59)
1971	840.00	5,403.14	2,146.56	(6,709.70)
1972	1,091.80	4,480.51	2,128.57	(5,518.08)
1973	2,440.58	6,061.31	4,332.88	(7,953.61)
1974	3,138.30	4,199.84	2,916.44	(3,977.98)
1975	3,098.00	6,518.40	2,689.68	(6,110.08)
1976	6,032.00	5,888.88	2,931.81	(2,788.69)
1977	7,165.00	6,106.62	2,667.90	(1,609.52)
1978	10,085.18	6,678.44	2,731.00	675.74
1979	11,455.00	7,616.29	2,050.78	1,787.93

During substantially all of the period of ownership, the taxpayers had their property listed for rent with one or more agents in Hawaii and advertised in newspapers. They also relied on word-of-mouth publicity. During 1970 and 1971, the property was listed with nine travel agencies in Oklahoma City and with two parties in Hawaii. In 1973, the taxpayers completely remodeled the condominium and purchased a new car for the use of potential lessees. They made an advertising album and began using newspaper advertising with greater frequency. In 1974, 1975, and 1976, they rented the condominium for 49 days, 48 days, and 85 days, respectively. Although the Internal Revenue Service characterized the taxpayers' efforts to obtain rentals of the apartment as spasmodic and half-hearted, the court found that they had engaged in the holding of the condominium for profit.

The Commission finds that the petitioner's efforts to obtain renters for his property fall short and that he has failed to carry his burden of proof that he was engaged in the rental activity for a profit.

The next issue to be dealt with concerns the itemized deductions claimed by the petitioner for 2001 and 2003. The auditor found that the standard deduction was more beneficial to the petitioner than was the allowance of the itemized deductions which were verified by the petitioner. The petitioner has not provided the Commission with any further documentation to establish his right to additional deductions. Therefore, the Commission finds that he has failed to carry his burden of proof with regard to this issue.

The last issue protested by the petitioner is the imposition of penalty. The auditor asserted the delinquency (25 percent) penalty for each of the years. The authority for the penalty is set out in Idaho Code § 63-3046(c) which stated, in part:

(1) In the event the return required by this chapter is not filed on or before the due date (including extensions) of the return, there may be collected a penalty of five percent (5%) of the tax due on such returns for each month elapsing after the due date (including extensions) of such returns until the return is filed.

The penalty was limited by Idaho Code § 63-3046(g) to 25 percent of the tax.

The petitioner did not file Idaho income tax returns. On June 23, 2006, the auditor sent the petitioner a notice of deficiency regarding 2001, 2002, and 2003. The return for the most recent of those years was past due by over two years. The petitioner had filed Idaho income tax returns for 1999 and 2000.

The petitioner concedes that he failed to file Idaho income tax returns for the years in question. He states that he filed federal returns and, therefore, the Commission had access to the necessary information to determine his liability. He asserts that, “[p]enalties should only be imposed on deliberate, deceitful [sic] acts designed to mislead or acts of premeditated fraud against the State of Idaho. I had my taxes completed by a tax expert, CPA who failed to inform me of conditions surrounding my situation. My failure to file was completely innocent without

any fault or intent to defraud. Under these circumstances the penalties should be waived with only interest applied.”

The penalty imposed was for the delinquency of the filing of the return. The returns in question were clearly filed delinquent. The Commission finds insufficient cause to justify abatement of the penalty.

WHEREFORE, the Notice of Deficiency Determination dated June 23, 2006, is hereby APPROVED, AFFIRMED, AND MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the petitioner pay the following tax and interest (computed to January 31, 2007):

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2001	\$1,320	\$332	\$378	\$2,030
2002	1,345	336	298	1,979
2003	1,335	334	225	<u>1,894</u>
			TOTAL DUE	<u>\$5,903</u>

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the petitioner's right to appeal this decision is enclosed with this decision.

DATED this ____ day of _____, 2006.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2006, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[REDACTED]

Receipt No.
